Financial Statement Data

Maryland Economic Development Corporation Financial Statement
Fiscal 2010-2012
($ in Thousands)

	2010	2011	2012	Change 2011-2012
Total Assets	$724,063	$679,110	$647,302	-$31,808
Total Liabilities	887,572	872,539	864,373	-8,166
Net Assets (Deficit)	**-$163,509**	**-$193,429**	**-$217,071**	**-$23,642**
Total Operating Revenue	$125,461	$129,982	$130,746	$764
Total Operating Expenses	113,320	118,457	118,657	200
Operating Income Subtotal	**$12,141**	**$11,525**	**$12,089**	**$564**
Non-operating Revenues and Expenses	-$44,578	-$41,444	-$35,730	$5,714
Net Income (Deficit)	**-$32,437**	**-$29,920**	**-$23,642**	**$6,279**

Change in Net Assets (Deficit) and Income by Source
Fiscal 2010-2012
($ in Thousands)

	2010	2011	2012	Change 2011-2012
Operating Facilities Net Assets	-$176,378	-$206,274	-$228,463	-$22,189
Other Operations Net Assets	12,868	12,845	11,392	-1,453
Net Assets (Deficit)	**-$163,509**	**-$193,429**	**-$217,071**	**-$23,642**
Operating Facilities Net Income	-$27,604	-$29,897	-$22,189	$7,708
Other Operations Net Income	-4,832	-23	-1,453	-1,430
Net Income (Deficit)	**-$32,437**	**-$29,920**	**-$23,642**	**$6,279**

Note: Other operations are comprised of property and equipment rental and consultant and management fees.

Source: Maryland Economic Development Corporation financial statements

Note: Numbers may not sum to total due to rounding.

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- The Maryland Economic Development Corporation's (MEDCO) net income deficit totaled -$23.6 million for fiscal 2012, a decrease of about $6.3 million. Operating income for fiscal 2012 was positive at $12.1 million, which is a key indicator of economic health. Noncash expenses, such as depreciation, and non-operating items, such as interest expense, cause the income and assets deficits, and these deficits are not uncommon for real estate projects. Each year that the net income deficit persists, the corporation's equity position declines. The net assets deficit grew to -$217,071 million in fiscal 2012.

- The corporation's net asset deficit is attributable to the accumulated losses of its operating facilities. The operating facilities' net income deficit decreased by $7.7 million in fiscal 2012. The corporation also experienced a net income deficit of $1.5 million in its other operations.

Analysis in Brief

Overall Financial Position

Operating Revenues Continue to Exceed Operating Expenses: The corporation's net asset deficit has grown to -$217.1 million. However, operating revenues continue to exceed operating expenses. Operating income grew approximately $564,000 in fiscal 2012.

MEDCO's Assets Exclusive of Operating Facilities Are Relatively Stable: Exclusive of operating facilities, MEDCO had $11.4 million in net assets in fiscal 2012, less than the 10-year average of $16.3 million. In fiscal 2012, MEDCO provided funding for six new projects.

Operating Facilities Financial Position

Net Assets Continue to Decrease: Operating facilities' net assets decreased by $22.2 million in fiscal 2012. This decrease is less than the decrease experienced in fiscal 2011.

Operating Income Increased in 2012; Four Projects Posted a Loss: Operating facilities' income was $11.6 million in fiscal 2012, an increase of $3.6 million. Four projects showed a loss, and two projects were defined as "watch" projects in the corporation's financial statement. **The Department of Legislative Services (DLS) recommends that MEDCO comment on the designation of the Chesapeake Bay Conference Center and the University of Maryland, Baltimore housing project as "watch" projects.**

Other Issues

Sale of Rocky Gap Resort: The Rocky Gap facility, as an operating project of the corporation, represented a drain on MEDCO's financial position. As part of the awarding of a State gaming license, the facility was sold to private interests in August 2012. **DLS recommends that the corporation brief the budget committees on how the sale of the Rocky Gap facility will impact its finances and plans for further investments.**

Legislative Audit: MEDCO is constituted as a public instrumentality of the State. As such, it is subject to a legislative audit every three years. In December 2012, an audit was released by the Office of Legislative Audits. Only one finding was cited in the audit.

New Operating Projects: In fiscal 2013, the corporation added new operating projects to its portfolio: housing facilities at Towson University and Salisbury University. **DLS further recommends that the corporation comment on its plans for expanding its operating project portfolio.**

Recommended Actions

1. Nonbudgeted.

Operating Budget Analysis

Program Description

The Maryland Economic Development Corporation (MEDCO) is a nonbudgeted entity that allows the State to own or develop property for economic development purposes. MEDCO was created in 1984 with the mission to help expand, modernize, and retain existing Maryland business and to attract new business to the State.

MEDCO purchases or develops property that is leased to others under favorable terms. MEDCO also makes direct loans to companies throughout the State to maintain or develop facilities, and it often serves as the conduit for loans administered by the Department of Business and Economic Development (DBED). MEDCO issues bonds to raise funds for its loans. The bond debt consists primarily of revenue bonds and notes payable to government agencies such as DBED. The debt represents non-recourse obligations because MEDCO is not liable to bondholders and lenders in the event of a project or borrower default. Each project must have self-supporting revenues, and no projects are cross-collateralized. As a result, MEDCO debt is not debt of the State, and there is no implied State guaranty or State obligation to protect bondholders from losses.

MEDCO has been involved in 240 projects through fiscal 2012. Of these, MEDCO owns and operates 14 as operating facilities, meaning the corporation is involved in management decisions and has a hand in ensuring successful daily operations. For other projects, MEDCO serves as an arms-length financing entity.

The corporation is governed by statute under the Economic Development Article, Sections 10-101 though 10-132. A 12-member board of directors oversees and approves actions pertaining to the corporation's affairs and appoints the executive director. The Secretaries of DBED and the Maryland Department of Transportation serve as ex-officio voting members. MEDCO's activities complement the marketing and financing programs of DBED. There are currently 10 full-time and 1 part-time professional staff members.

In 2001, MEDCO's statutory authority was amended to be more consistent with the Maryland Economic Development Revenue Bond Act and economic development revenue bond enabling legislation that is in effect in other states competing for opportunities. MEDCO's legislative purpose now is to (1) relieve the conditions of unemployment; (2) encourage increased business activity and commerce and a balanced economy; (3) assist in the retention and attraction of new business activity; (4) promote economic development; and (5) generally promote the present and prospective health, happiness, safety, right of employment, and general welfare of State residents.

MEDCO's Overall Financial Position

Operating Revenues Exceed Operating Expenses

MEDCO operates 14 facilities, and revenue from those facilities contributes to the corporation's bottom line. As shown on page 1 of this analysis, operating revenues did not cover both operating and non-operating expenses; therefore, the corporation had a net income deficit of -$23.6 million in fiscal 2012. This is a smaller income deficit when compared to the losses experienced in fiscal 2011. Operating revenues ($130.7 million) continue to exceed operating expenses ($118.7 million).

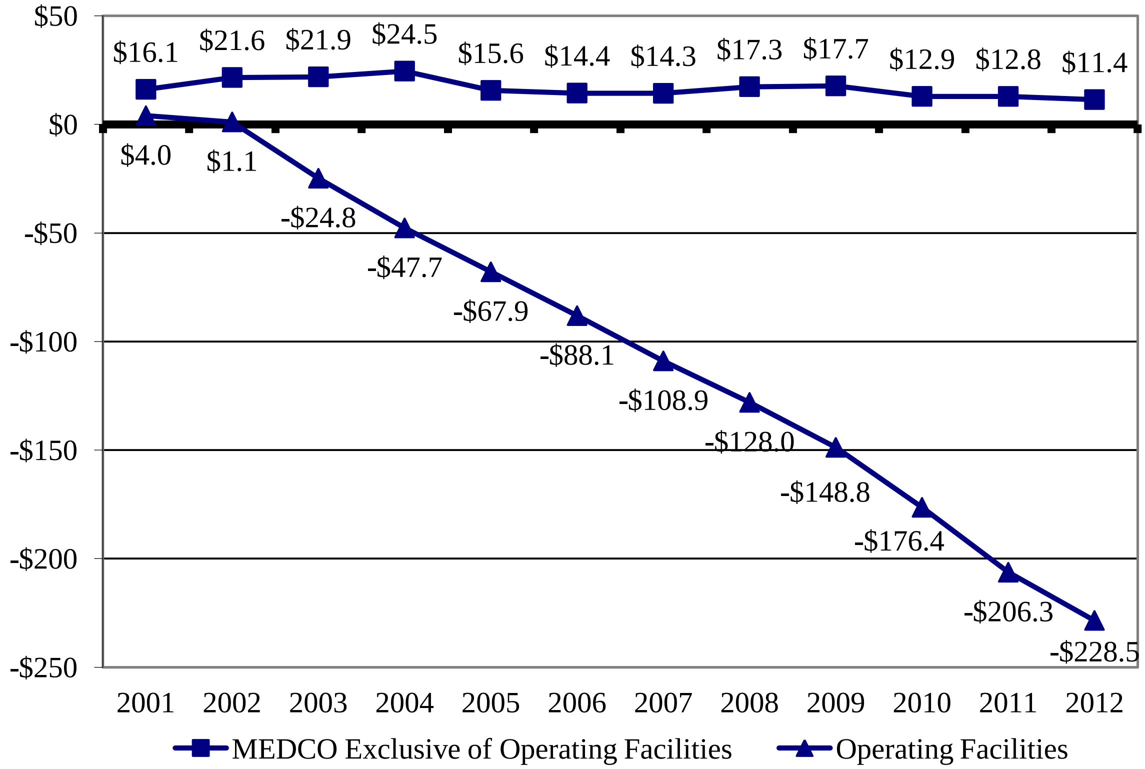
Each year that the net income deficit persists, the corporation's equity position declines. The net assets deficit grew to -$217.1 million in fiscal 2012, as shown on page 1. The corporation reports that the growing net assets deficit is not a significant concern as long as operating revenues exceed cash operating expenses. MEDCO reports that net losses and assets deficits are not uncommon for real estate companies. With these companies, the market value of the assets generally exceeds the book value, and MEDCO says that real estate investors look at market value or, more specifically, cash flow coverage rather than book value.

MEDCO's Assets Exclusive of Operating Facilities Are Relatively Stable

Exhibit 1 shows the value of MEDCO's net assets with operating facilities extracted. MEDCO, exclusive of operating facilities, had $11.4 million in net assets in fiscal 2012. The balance has averaged $16.3 million for the last 10 years. These funds represent the accumulation of excess fees over operating expenses that MEDCO attains as it conducts financing transactions each year. In fiscal 2012, MEDCO provided financing for six new projects.

MEDCO has 14 operating facilities in its portfolio. The net assets deficit for these facilities grew to -$228.6 million in fiscal 2012, as shown in Exhibit 1. The operating net assets deficit began to grow dramatically in fiscal 2003. It was at this time that MEDCO greatly expanded its operating facility portfolio, including the Chesapeake Bay Conference Center and several university housing projects. The net assets deficit is a direct result of adding new operating real estate facilities. MEDCO's operating projects often have net income deficits (as explained above), and with the addition of each operating project, a net income deficit is added to the accounts, which in turn adds to the overall net assets deficit.

Exhibit 1
MEDCO Net Assets
Fiscal 2001-2012
($ in Millions)



MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Operating Facilities Financial Position

Net Assets Continue to Decrease

Exhibit 2 shows the increases and decreases in MEDCO's net assets by project. Operating facilities' net assets decreased by $23.6 million in fiscal 2012. This decrease is less than the decrease experienced in fiscal 2011. The primary driver of the decreased assets is depreciation. However, in fiscal 2012, the decline in net assets was partially offset by capital improvements at several of the corporation's operating facilities.

Exhibit 2
MEDCO Increase (Decrease) in Net Assets by Project
Fiscal 2010-2012

	2010	2011	2012	Total Net Assets (Deficit) at End of 2012
University Student Housing				
Morgan State University	$101,138	-$605,226	$713,432	-$6,243,484
Bowie State University	-933,396	-51,143	86,099	-5,201,275
Frostburg State University	-221,928	40,818	-324,435	-3,228,587
Salisbury University	-253,562	-212,320	-294,519	-3,039,188
Towson West	-1,103,721	-853,684	-755,126	-3,285,990
University of Maryland, Baltimore	-1,131,682	-867,496	-504,540	-9,929,497
University of Maryland Baltimore County	144,486	286,207	470,066	-2,372,763
University of Maryland, College Park Housing	-2,551,065	-3,125,429	-1,862,265	-16,516,342
University Village at Sheppard Pratt	-753,502	-666,804	-708,274	-9,726,403
Subtotal	***-$6,703,232***	***-$6,055,077***	***-$3,179,562***	***-$59,543,529***
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	-$14,383,265	-$14,526,159	-$13,895,337	-$116,379,934
Shady Grove Innovation Center	54,794	158,050	-309,850	5,068,525
Rockville Innovation Center	-416,970	-551,423	-144,998	-196,678
Rocky Gap Golf Resort	-5,667,383	-6,147,219	-5,769,162	-59,970,699
University of Maryland, College Park Energy	-502,753	-2,807,083	1,081,999	3,277,181
Subtotal	***-$20,915,577***	***-$23,873,834***	***-$19,037,348***	***-$168,201,605***
Subtotal Operating Facilities	**-$27,618,809**	**-$29,928,911**	**-$22,216,910**	**-$227,745,134**
MEDCO Exclusive of Operating Facilities	**-$4,832,301**	**-$23,132**	**-$1,453,158**	**$11,392,196**
Elimination (Accounting Adjustment)	**$14,514**	**$32,432**	**$28,364**	**-$717,767**
Grand Total	**-$32,436,596**	**-$29,919,611**	**-$23,641,704**	**-$217,070,705**

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Operating Income Increased in 2012; Four Projects Posted a Loss

Exhibit 3 shows MEDCO operating income and loss by project. The data indicates whether projects are bringing in enough revenues to cover annual operating expenses. Operating facilities' income increased to $11.6 million in fiscal 2012, compared to $8.0 million in 2011. However, four projects posted a loss in fiscal 2012, compared to three in the previous year. This is due to the fact that Shady Grove Innovation Center posted a loss instead of a gain in fiscal 2012, as has been the case in past years. All of the university student housing projects posted gains in each year shown, as did the University of Maryland, College Park energy project.

Exhibit 3
MEDCO Operating Income (Loss) by Project
Fiscal 2010-2012

	2010	2011	2012
University Student Housing			
Morgan State University	$2,303,309	$1,560,344	$2,851,454
Bowie State University	182,418	567,778	1,149,554
Frostburg State University	739,752	986,950	593,641
Salisbury University	485,229	512,435	417,575
Towson West	748,156	909,926	984,468
University of Maryland, Baltimore	759,907	998,838	1,330,651
University of Maryland Baltimore County	1,511,367	1,494,918	1,568,526
University of Maryland, College Park Housing	4,238,501	4,865,552	6,089,032
University Village at Sheppard Pratt	1,093,211	1,133,079	1,169,786
Subtotal	***$12,061,850***	***$13,029,820***	***$16,154,687***
Other Facilities			
Chesapeake Bay Conference Center (Hyatt Cambridge)	-$3,699,379	-$3,577,916	-$3,001,517
Shady Grove Innovation Center	-51,777	102,744	-282,238
Rockville Innovation Center	-489,791	-633,227	-342,328
Rocky Gap Golf Resort	-3,811,819	-4,307,611	-3,887,819
University of Maryland, College Park Energy	3,534,151	3,348,641	2,952,566
Subtotal	***-$4,518,615***	***-$5,067,369***	***-$4,561,336***
Subtotal Operating Facilities	**$7,543,235**	**$7,962,451**	**$11,593,351**
MEDCO Exclusive of Operating Facilities	**$4,583,344**	**$3,529,674**	**$467,061**
Elimination (Accounting Adjustment)	**$14,514**	**$32,432**	**$28,364**
Grand Total	**$12,141,093**	**$11,524,557**	**$12,088,776**

MEDCO: Maryland Economic Development Corporation

Note: MEDCO sold Chesapeake Hills Golf Course to Calvert County in fiscal 2008.

Source: Maryland Economic Development Corporation

According to the corporation's financial statement, there are two operating projects identified in fiscal 2012 as "watch" projects for failure to meet debt coverage ratios. Both of these projects have been cited in previous financial statements as problematic. Each of these and all other MEDCO projects need to be considered on its own merits because no MEDCO projects are cross-collateralized, and each project must support itself with its own revenues.

- **Chesapeake Bay Conference Center:** The Chesapeake Bay Conference Center (CBCC) is located in Dorchester County. It houses a hotel, golf course, and conference facilities. Although it is experiencing an increase in revenue from its operations, the project is unable to meet its required debt coverage ratio. MEDCO secured a management consultant to suggest changes in pricing and expense reductions in order to bring the ratio into compliance.

- **University of Maryland, Baltimore:** The housing project at the University of Maryland, Baltimore (UMB) is the other project that is considered problematic in the financial statements.

MEDCO became involved in university housing projects in 1999 when the University System of Maryland approached the corporation because the customary owner, the Collegiate Housing Foundation, came under investigation by the Internal Revenue Service. MEDCO studied the cash flow potential of the projects and found it to be solid.

MEDCO believes that university housing is a good fit for its financing, and it plans to continue to become involved in such projects. The corporation reports that the universities, in some instances, do not want to own and operate the facilities themselves; yet, a university campus is not necessarily an ideal environment for a traditional private real estate entity.

MEDCO has explained that it is not unusual for its real estate projects to show deficits, and it cautions that in the case of university housing, deficits are essentially guaranteed. There is a provision in the bond issuances that specifies that excess cash goes back to the university as additional rent or a ground lease rather than into the projects' equity. MEDCO reports that university housing bond issuances usually are structured this way, and it is for this reason that housing bonds are at the low end of investment grade ratings.

Department of Legislative Services (DLS) recommends that MEDCO comment on its operating projects and specifically on the continued designation of CBCC and UMB as "watch" projects.

Other Issues

Sale of Rocky Gap Resort

Rocky Gap consists of a 215-room hotel and conference center and an 18-hole Jack Nicklaus Signature golf course situated on about 260 acres within Rocky Gap State Park. This State project was approved in 1996 and was funded with a variety of State and local sources, including MEDCO revenue bonds ($31.3 million); State general obligation bonds ($10.9 million); Department of Business and Economic Development grants and loans ($4 million); and bonds issued by Allegany County ($4.5 million).

The facility has incurred significant net operating losses, totaling $3.9 million in fiscal 2012 alone, as shown in Exhibit 3. Several attempts were made to stem the project's losses including further cash infusions, restructured debt, foregone ground rent, and a line of credit from MEDCO.

Legislation adopted during the 2007 special session authorized the Rocky Gap facility to become one of the State's five locations for video lottery terminals (VLT). A request for proposal (RFP) for a VLT facility at Rocky Gap was issued in 2008. After rejecting (in February 2009) the single proposal received, the Video Lottery Facility Location Commission (Location Commission) made several recommendations to the General Assembly related to the Allegany County location with the hope that the location could be made more attractive to potential applicants. In response, Chapter 624 was enacted in 2010. Contingent upon the purchase of Rocky Gap by the licensee, 2.5% of VLT proceeds from the Allegany County facility, for the first five years of operations, that would otherwise be distributed to other purposes would instead be distributed to the Allegany County facility licensee. Subsequent to the enactment of Chapter 624, the Location Commission issued a new RFP for the Allegany County location in July 2010, but no proposals were received by the November 2010 deadline.

In an effort to provide further incentives for potential applicants for the Allegany County location, Chapter 240 of 2011 made several changes, including increasing the Allegany County licensee's share of the proceeds to 50% for the first 10 years of operations. The Location Commission issued another RFP for Allegany County in June 2011 and received three proposals. In April 2012, the location commission awarded a license to Evitts Resort LLC, with the condition that the licensee purchase the Rocky Gap facility.

In June 2012, the Board of Public Works approved the transfer of the ground lease from MEDCO to the VLT licensee. The purchaser paid $6,775,000 for the acquisition, while MEDCO contributed $3.0 million ($1.5 million of which will be repaid once gaming starts at the facility). From this amount, bondholders will be paid, once other liabilities of the facility have been settled. All liabilities due to DBED and the Department of Natural Resources were forgiven.

As a result of this sale, MEDCO's net income and net asset position should improve.

DLS recommends that the corporation brief the budget committees on how the sale of the Rocky Gap facility will impact its finances and plans for further investments.

Legislative Audit

The corporation is constituted as a public instrumentality of the State. As such, it is subject to a legislative audit every three years. In December 2012, an audit was released by the Office of Legislative Audits. The auditors cited only one finding related to processing cash receipts. It was recommended that MEDCO adopt certain accountability measures to ensure proper handling of receipts. It is worth noting that two findings from the corporation's previous legislative audit have been addressed.

In response to the new finding, the corporation agreed to the finding and proposed several remedies including unique usernames and passwords for certain employees.

New Operating Projects

As the Rocky Gap Resort exits the portfolio of the corporation's operating projects, the corporation took steps to acquire new projects. In July 2012, the corporation acquired Millennium Hall at Towson University using $15.6 million in revenue bonds. This is a 420-bed student residential housing facility. Similarly, in July 2012, MEDCO also acquired University Park I Student Housing at Salisbury University. This building houses 578 beds for students. The corporation issued $14.7 million in revenue bonds for this project.

DLS further recommends that the corporation comment on its plans for expanding its operating project portfolio.

Recommended Actions

1. Nonbudgeted.